(4)

Supreme Court, U.S.
FILED
OCT 6 1992
OFFICE OF THE CLERK

No. 92-363

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

995 FIFTH AVENUE ASSOCIATES, L.P.,

Petitioner,

—v.—

NEW YORK STATE DEPARTMENT OF TAXATION AND FINANCE; JAMES W. WETZLER, As Commissioner of Taxation and Finance; and EDWARD V. REGAN, As Comptroller of the State of New York,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

Joshua J. Angel
(Counsel of Record)
Leonard H. Gerson
Ira R. Abel
ANGEL & FRANKEL, P.C.
366 Madison Avenue
New York, New York 10017-3191
(212) 286-0100

Counsel for Petitioner

BEST AVAILABLE COPY

TABLE OF CONTENTS

PAGE

TABLE OF CONTENTS i

TABLE OF AUTHORITIES..... ii

ARGUMENT..... 2

CONCLUSION..... 9

TABLE OF AUTHORITIES

Cases PAGE

CCA Partnership v. Director of Revenue (In re CCA Partnership), 70 Bankr. 696 (Bankr. D. Del.), *aff'd*, 72 Bankr. 765 (D. Del.), *aff'd*, 883 F.2d 303 (3d Cir. 1987) 4

City of New York v. Baldwin League of Independent Schools (In re Baldwin League of Independent Schools), 110 Bankr. 125 (S.D.N.Y. 1990) 4

City of New York v. Jacoby-Bender, Inc. (In re Jacoby-Bender, Inc.), 758 F.2d 840 (2d Cir. 1985) 4

City of New York v. Smoss Enterprises Corp. (In re Smoss Enterprises Corp.), 54 Bankr. 950 (E.D.N.Y. 1985) .. 4

In re Cantrup, 53 Bankr. 104 (Bankr. D. Col. 1985) 4

In re Permar Provisions, Inc., 79 Bankr. 530 (Bankr. E.D.N.Y. 1987) 4

Other Authorities

N.Y.S. Dept. of Taxation and Finance, *Questions and Answers—Gains Tax on Real Property Transfers*, p. 27, Publication 588 (November 1984) 2

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

Docket No. 92-363

995 FIFTH AVENUE ASSOCIATES, L.P.,

Petitioner,

—v.—

NEW YORK STATE DEPARTMENT OF TAXATION AND FINANCE; JAMES W. WETZLER, As Commissioner of Taxation and Finance; and EDWARD V. REGAN, As Comptroller of the State of New York,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

The Second Circuit reversed the decisions of the bankruptcy court and the district court, and found that the tax imposed by N.Y. Tax Law §§ 1440 *et seq.* (the "Gains Tax") was not a "stamp tax or similar tax," and thus did not fall within the exemption provided by § 1146(c) of the Bankruptcy Code. It arrived at this conclusion by revising the test applied by the district court for defining a "stamp tax or similar tax." The inability of the respondents to provide even a plausible defense of this revised test reflects the indefensible nature of the court of appeals decision and the need for this Court's review.

ARGUMENT

Respondents admit that "large sums of money are at stake in this case, and the decision of the court of appeals may have an economic impact beyond the borders of New York. . . ." Brief in Opposition at 5. For example, Bloomingdale's flagship store in Manhattan is a prized asset in a bankruptcy case in Ohio, *In re Federated Department Stores, Inc.*, S.D. Ohio, No.1-90-00130. Nevertheless, respondents deny the issues raised in the Petition will have more than local significance, because bankruptcy courts outside of New York would be bound to follow the Second Circuit's decision. Brief in Opposition at 5-6. Obviously, if an unjustifiable opinion by the Second Circuit will control the decisions of bankruptcy courts across the nation, this factor provides only more, not less reason for this Court to grant the Petition.

Respondents also claim that this case is only of local importance because "[i]t is indisputable that only New York has a tax such as the gains tax." Brief in Opposition at 5. An explanation provided in New York's official publication for administering the Gains Tax demonstrates the fallacy in this reasoning:

> 75. Deductibility of the Gains Tax
>
> Q. Is the gains tax deductible from both federal and state income tax?
>
> A. In light of Federal Revenue Ruling 80-121 which held that *a similar Vermont land gains tax* constituted a "transfer tax" and is deductible for purposes of computing adjusted gross income under section 164(a) of the Internal Revenue Code, it is the Department's position that Article 31-B of the Tax Law also constitutes a transfer tax, and is therefore deductible. However, the Internal Revenue Service will ultimately determine its deductibility for federal tax purposes which will then apply for state tax purposes.

N.Y.S. Dept. of Taxation and Finance, *Questions and Answers—Gains Tax on Real Property Transfers*, p.27, Publication 588 (November 1984) (emphasis added).

This statement and analysis in New York's official publication on the Gains Tax, which is based upon the "similar" natures of the Gains Tax and the Vermont land gains tax, contradicts the claim in the Brief in Opposition that the characteristics of the Gains Tax are so singular so as to make it *sui generis*. Moreover, it is the approach and unjustifiable test that the Second Circuit has created for defining a "stamp tax or similar tax" which creates the legal question which warrants this Court's attention, not simply the application of the § 1146(c) exemption to the Gains Tax.

In attempting to deny the national significance of the opinion below, respondents have distorted its reasoning and language. Respondents assert that the opinion below states: "Section 1146(c) does not accord greater tax relief to debtors than was formerly available. (13a, n.2)." Brief in Opposition at 4-5, n.4. However, footnote 2 in the decision below reads:

> The report of the House Judiciary Committee stated that "[s]ection 1146(c) of title 11 broadens the exemption to any stamp or similar tax." H.R. Rep. No. 595, Cong., 1st Sess. 281(1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6238. We disagree with the district court to the extent it concluded that this statement reflects Congress's intent that the words "stamp or similar tax" be read broadly to accord greater tax relief for debtors. Instead, we regard this statement as a simple declaration that the new provision, *§ 1146(c), enlarges the former exemption under § 267 to include taxes similar to stamp taxes.*

(13a,n.2) (emphasis added).[1] No logical reading of this footnote could result in the conclusion that the Second Circuit stated: "Section 1146(c) does not accord greater tax relief to debtors than was formerly available."

Respondents are desperately seeking to avoid giving footnote 2 a natural reading, because in the decision the Second Circuit simply failed to analyze the meaning of the term "similar tax."

---

1 The pages of the appendix to the Petition are referred to as "___a".

Although respondents claim that the Second Circuit "interpreted the words used by Congress, 'stamp tax or similar tax' in accordance with 'their ordinary, contemporary, common meaning,' " Brief in Opposition at 2-3, such a claim is another distortion of the opinion. Respondents do not question that such an approach is mandated by this Court's earlier opinions. However, in its decision it is only the term "stamp tax" that the Second Circuit attempts to give an " 'ordinary, contemporary, common meaning.' " (14a-15a). As is more fully described in the Petition, unlike its approach to understanding the meaning of the term "stamp tax," the Second Circuit simply ignored interpreting the term "similar tax" once it concluded that no definition was available from a review of the legislative history. In an attempt to conceal this critical failure in the decision the respondents misquote the decision in the Brief in Opposition.

This failure by the Second Circuit is of critical importance because it was by adding the term "similar tax" that Congress broadened the earlier Bankruptcy Act's stamp tax exemption. *City of New York v. Baldwin League of Independent Schools (In re Baldwin League of Independent Schools)*, 110 Bankr. 125, 126-27 (S.D.N.Y. 1990). This recognition of an expansion of the exemption was central to the Second Circuit's earlier decision interpreting § 1146(c), *City of New York v. Jacoby-Bender, Inc. (In re Jacoby-Bender, Inc.)*, 758 F.2d 840 (2d Cir. 1985). Courts across the nation have utilized *Jacoby-Bender* as a basis for defeating attempts by governmental entities to impose a narrow interpretation on the § 1146(c) exemption. *In re Cantrup*, 53 Bankr. 104 (Bankr. D. Col. 1985); *CCA Partnership v. Director of Revenue (In re CCA Partnership)*, 70 Bankr. 696 (Bankr. D. Del.), *aff'd*, 72 Bankr. 765 (D. Del.), *aff'd*. 883 F.2d 303 (3d Cir. 1987); *City of New York v. Smoss Enterprises Corp. (In re Smoss Enterprises Corp.)*, 54 Bankr. 950 (E.D.N.Y. 1985); *In re Permar Provisions, Inc.*, 79 Bankr. 530 (Bankr. E.D.N.Y. 1987); *City of New York v. Baldwin League of Independent Schools (In re Baldwin League of Independent Schools)*, 110 Bankr. 125 (S.D.N.Y. 1990). Rather than demonstrating that the decision below is only of local significance, by

stating that the Second Circuit now reads § 1146(c) as not "accord[ing] greater tax relief to debtors than was formerly available," the respondents have demonstrated how the decision below will be used to impose an unreasonably narrow interpretation on the § 1146(c) exemption in contrast to the position repeatedly taken by other courts, including the Second Circuit itself in *Jacoby-Bender*. The decision thus invites unwarranted court challenges and the manipulation of state tax laws in an effort to circumvent the § 1146(c) exemption.

Respondents claim that the Petition did "not challenge the court's definition of the characteristics of a stamp tax," but only disagreed with "the relative importance of both the common and distinguishing characteristics between the court's definition of a stamp tax and the gains tax." Brief in Opposition at 6. This statement reflects the inaccurate and disingenuous character of the Brief in Opposition. The Petition focused upon three characteristics identified by the Second Circuit—the alleged imposition of the Gains Tax only upon transactions which yield a profit, the base upon which the tax is imposed, and the Gains Tax's ten percent rate—because it was these three characteristics which the Second Circuit found as taking the Gains Tax outside of the § 1146(c) exemption. *See* 15a-20a and Brief in Opposition at 3. The "relative importance" of these characteristics is crucial because if these alleged differences are non-existent or inconsequential, allowing them to determine whether the Gains Tax falls within the § 1146(c) exemption essentially eliminates the "similar tax" exemption from the Bankruptcy Code. The basic fault in the decision below is that it simply identified what it believed were three differences without weighing their significance, notwithstanding the language in § 1146(c) which states that taxes which are "similar" to stamp taxes fall within the exemption.

As the Second Circuit failed to analyze the significance of the alleged differences it identified, the respondents are forced to rely upon sophistry to support the decision. The Brief in Opposition states:

> For example, petitioner argues that it was misleading for the court of appeals to focus *only* on the tax rate. (9). This argument is belied by the decision below. The tax rate was only one of five factors considered by the court in determining whether the gains tax was a "stamp tax or similar tax."

Brief in Opposition at 6. Of course, Fifth Avenue Associates never argued that the Second Circuit's decision was based only upon a finding that the Gains Tax was imposed at a high rate—in excess of one percent, the rate claimed by the Second Circuit to be "typical" of a stamp tax. Instead, in response to one of three characteristics relied upon by the court of appeals to distinguish the Gains Tax from a stamp tax, Fifth Avenue Associates maintained that simply addressing the relatively higher rate of the tax was misleading. When one takes into account the narrower base upon which the Gains Tax is imposed, the higher rate does not result in a tax with an order of magnitude which can be distinguished from a "stamp tax or similar tax." *See* Petition at 9. Respondents are unable to justify the significance the Second Circuit attributed to the Gains Tax's higher rate, so they simply attempt to defend the opinion in the Brief in Opposition by misstating the arguments of Fifth Avenue Associates.

Equally distorted is respondents' defense of the Second Circuit's position that the Gains Tax is not a "stamp tax or similar tax" because it is imposed on neither " 'the par value of the security, the consideration in the deed, or the value of the property that is the subject of the transaction.' " Brief in Opposition at 6. Although Fifth Avenue Associates cited many exempt taxes which fail to satisfy any of these criteria because the value of assumed liens is excluded in calculating the amount of consideration, respondents state:

> This conclusion is flatly contradicted by the RETT statute (Tax Law § 1402) which defines the consideration to be taxed. The stamp tax statutes of other States cited by the petitioner (10, 11) similarly define the consideration to be

> taxed. Thus, there is no possibility of the nation-wide confusion imagined by petitioner. (11).

Id. Obviously, the confusion which may be engendered by the Second Circuit's decision will not stem from the failure of the relevant state statute to define the consideration. Confusion will arise because the definition of the consideration to be taxed will not conform to the Second Circuit's requirements for defining a tax which falls within the § 1146(c) exemption.

Fifth Avenue Associates' concern for the possibility of "nation-wide confusion" is not "imagined." When the Second Circuit issued its initial opinion in this case, major New York law firms warned their clients that the court's definition of a "stamp tax or similar tax" threatened the continued application of the § 1146(c) exemption to the New York City Real Property Transfer Tax. It was only after the Second Circuit amended its opinion to modify its initial requirement that a "stamp tax or similar tax" must have a rate of one percent or less, that this fear was allayed. However, the continuing dangers arising from the amended opinion are reflected in the inability of the respondents to defend the propositions upon which the decision is based.

The foremost proposition upon which the decision relied was the premise that the Gains Tax was "always contingent on the profitability of the underlying transaction." (19a). As Fifth Avenue Associates described in the Petition, in a recent joint study by The Association of the Bar of the City of New York and the New York State Bar Association, the Gains Tax was found to be imposed even when losses are incurred in a transfer. Petition at 12. The respondents claim this finding is irrelevant because "[n]owhere in the report . . . is there any mention of the gains tax being imposed when there is no gain, *as gain is statutorily defined.*" Brief in Opposition at 7, n.5 (emphasis added). Obviously, the relevant question is not whether gain exists as gain is defined by the statute. The issue is whether the statute defines real gain or whether the Gains Tax is imposed even when losses are incurred in a transaction. The respondents are unable to provide support for the central

proposition upon which the decision rests, so they rely repeatedly upon arguments which misstate the issue.

Finally, respondents claim that Fifth Avenue Associates improperly has requested that this Court decide whether the Gains Tax violates the doctrine of intergovernmental tax immunity. Brief in Opposition at 8. Again, the respondents have misrepresented the arguments in the Petition rather than responding to the issue raised. Fifth Avenue Associates has not asked this Court to decide whether the Gains Tax violates the Constitution. Instead, it has urged this Court to grant the Petition because by addressing the Second Circuit's faulty construction of § 1146(c) the Court may avoid the later necessity of deciding the delicate constitutional question arising from the Gains Tax's discriminatory treatment of secured lenders in bankruptcy.

The distortions and sophistry upon which respondents rely reflect the lack of substance in the Second Circuit's decision. Even respondents recognize the economic significance of the issue involved. The Second Circuit has inexplicably reversed its earlier approach to § 1146(c), and instead has imposed a narrow, ill-considered test which cannot withstand scrutiny. As the Second Circuit's decision in *Jacoby-Bender* influenced courts across the nation, so will its mischaracterization of the § 1146(c) exemption create major problems in reorganizations unless the decision is subject to this Court's review. In a period when public and private entities are mired in massive real estate collapses, this Court should not allow the Second Circuit's indefensible opinion to undermine reorganizations.

CONCLUSION

For the foregoing reasons, respondents' arguments in opposition to the petition for a writ of certiorari should be rejected and the writ should issue.

Respectfully submitted,

Joshua J. Angel
(*Counsel of Record*)
Leonard H. Gerson
Ira R. Abel
ANGEL & FRANKEL, P.C.
366 Madison Avenue
New York, NY 10017-3191
(212) 286-0100

October 6, 1992